RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

Since 1958 •

Post Office Box 1759, La Jolla, California 92038

26 Letters Per Year • $250 annually

Feb. 17, 1993 **LETTER 1115**

INFLATION?: Commodity cycles at a five-year bottom, lumber contracts going through the roof (up the limit every day), light crude oil over 20, gold edging up, palladium and platinum rising, new highs in American Barrick and Placer Dome, housing prices moving up, taxes going up along with the US cost-of-living -- and last but not least, Clinton asking for more economic stimulation. Prognosis -- deficits for as far out as the eye can see. The background for gold is the best in a decade.

THE MARKET: Ah, the **PTI,** that son-of-a-gun, it's been telling us the story all along. Of course, the PTI never tells us what or how or when -- it simply identifies the undercurrent, the true immediate trend of the market. As I've said ever since 1971 when I first included the PTI in these reports, "If the PTI embarks on a persistent uptrend, there's no way that the market will not follow. And the same is true if the PTI lapses into a persistent downtrend."

As for valuation, price/earnings ratios, contrary opinion, book value, short interest, the PTI takes no notice of any of these. The PTI deals strictly with price action. Every one of its eight components are based on price action.

The Dow Theory, that's a different story. The Dow Theory deals with values, yields, market phases, investor sentiment, AND, of course, price action. In these Letters I present my view of the market under Dow Theory, but I also include that remorseless, unemotional thin black line -- the PTI.

As you can see on the page 2 chart, the PTI, along with the advance-decline ratio, has been rallying to new highs. In fact, since October the rise in the PTI has been relentless. The advance has been telling us that the direction of the market is up. There was no other way to read it.

From a Dow Theory standpoint the picture is not nearly as pat. There's the problem of overvaluation, which I will go into later in the Letter. However, we do have --

New Highs in the Averages. On February 4 the Dow rallied above its June 1, 1992, peak, to close at a new record high. That high came one day after a new record high in the Transportation Average. On the face of it, this twin breakout to new highs in the Averages should be bullish. Nevertheless, caution is recommended.

But is there any need for caution? The answer is yes, and there are a few good reasons why -- aside from the simple fact of overvaluation. At this point I want to review some of the recent price action.

As stated, on February 3 the D-J Transportation Average rallied to close above its previous record high of 1532.01 struck on September 5, 1989. The new Transport high generated a good deal of excitement on Wall Street (I know because I received about 50 phone calls). Further excitement and bullishness was generated when, on the following day (February 4) the Dow closed above its own record high of last June 1.

How much bullishness should be accorded the breakout of both D-J Averages to new all-time highs? Ordinarily, I would say this was very bullish action. But there are some caveats.

Feb. 5 DJIA 3442.14; PTI 3723; A-D Ratio -5.86
Feb. 11 DJIA 3422.69; PTI 3724; A-D Ratio -5.92
Dow Yield: 3.02%; Dow Price/Earnings: 33.2
Dow 200-day MA: 3298; Dow 30-day MA: 3305
Dow Times Book Value: 2.64; PTI 89-day MA: 3641
Percentage of Undervalued Blue-chips: 8%
Low Risk Buy Index: +93

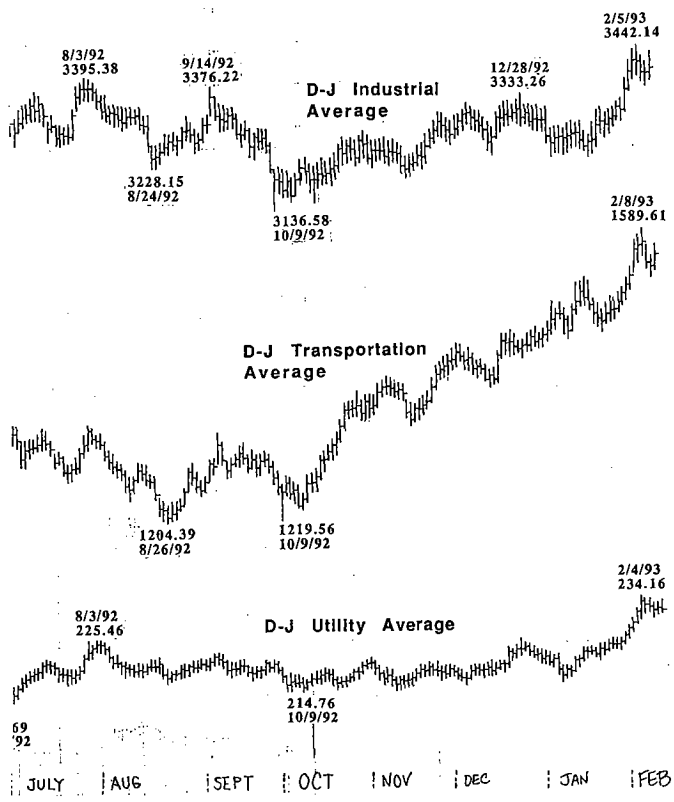
First, we are looking at a very old bull market. It's a bull market that began in 1974, although some students insist that it began in 1982. Either way, it's a bull market that's long in the tusks.

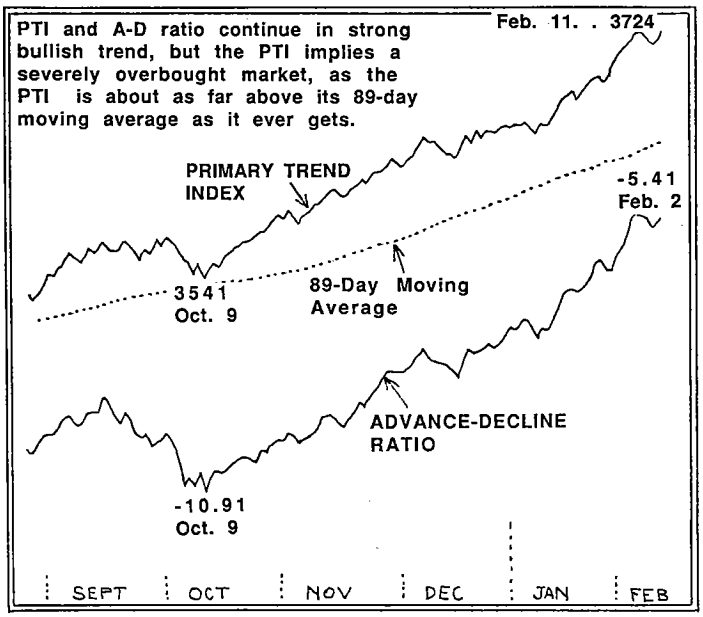
The initial bull signal (confirmation) in a new bull market, is by far the most important one. It's the one that tells us to load up on stocks. But there may be literally dozens of additional upside confirmations as the bull market moves along.

Each successive confirmation in a bull market should be accorded less authority -- until finally there will be an upside confirmation which will be the last one prior to the onset of the next bear market. At that point, detractors of Dow Theory will shout that "the Theory doesn't work," but these people never understood Dow's Theory in the first place, and their complaints are a product of their own ignorance.

Another question: What about the fact that the Transports rose to a new high (they confirmed) after a long lag of four years (the old Transport peak of 1532.01 was set in 1989)?

Interestingly, this same sequence occurred back in the bull market of the 1930s. At that time the D-J Rails (now the Transports) hit a high in 1933, and did not better that high until September of 1936. Robert Rhea, the great Dow Theorist of that time, wrote as follows




PTI and A-D ratio continue in strong bullish trend, but the PTI implies a severely overbought market, as the PTI is about as far above its 89-day moving average as it ever gets.
Feb. 11. . 3724
PRIMARY TREND INDEX
-5.41 Feb. 2
3541 Oct. 9
89-Day Moving Average
ADVANCE-DECLINE RATIO
-10.91 Oct. 9
SEPT
OCT
NOV
DEC
JAN
FEB

(Sept. 26, 1936): *"In the opinion of this writer, the fact that the Rails have finally bettered their 1933 highs is of no particular forecasting significance because of the extreme age of the older objective. No similar condition was ever recorded in the Averages. The event does, however, delight the students who demand complete fulfillment of every detail."*

In March 1937, six months after Rhea wrote the above, the 1932-37 bull market hit its final peak and died. A bear market took hold. By September 1937, the market had been cut in half.

Is this the kind of sequence we're looking at today? Frankly, it would not surprise me.

MORE ON VALUES: In the last Letter (statistical chart, page 3) I showed that since 1871 there have only been seven instances in which investors were so wildly bullish that they were willing to pay around $35 for one dollar of S&P dividends. Today investors are paying $36.30 for every dollar of S&P dividends. In my opinion, this is the operative fact in the market today. It's the single most important market fact of 1993.

To refresh your memory, these seven previous instances in which investors paid around $35 or more for one dollar of Dow dividends occurred in 1929, 1933, 1961, 1965, 1968, 1973 and 1987. Three of these periods were followed by crashes (1929, 1962, 1987) and the other four were followed by severe declines averaging 40% (or 25% if you leave out the extreme case of 1929).

Fact: Again I repeat that today it costs $36.30 to buy one dollar of S&P dividends. This constitutes a time-honored danger signal. It tells us where we are in the big picture. I don't know how long the market will remain in this area. I don't know whether the market will go somewhat higher. But the longer the market holds at this valuation or the higher it climbs from here, the more precarious the situation.

Why? Because if nothing else, large investors are judges of values. And when stocks sell at these exalted prices, large investors have always done one thing -- they have distributed stocks. There's nothing more powerful in the market than the accumulation or distribution of stocks by large, powerful, informed investment interests.

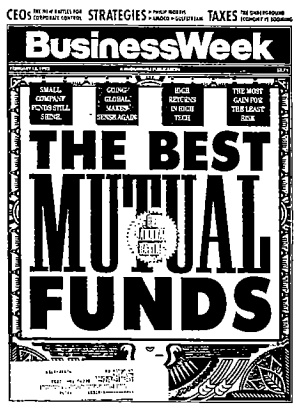
It is well to remember that at today's high valuations they don't raise a blazing red banner which says, "Halt, the market is too high, please sell." What happens is that when values become thin, investors begin to part with their wares. At first it doesn't show in the averages. Maybe only certain stocks or certain groups are distributed. But as the informed selling spreads (almost always while the news is good and while the public is buying heavily) the technical underpinnings of the market slowly deteriorate. Finally, selling overcomes buying and the bear takes over.

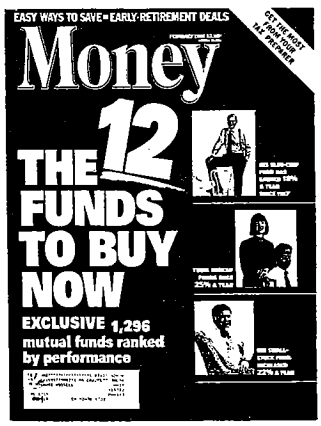
Here are a few more items that are worth considering. Today there are thousands of intelligent analysts who spend eight hours a day or more scrutinizing the market, studying stocks, studying statistics, studying charts. These analysts don't miss much. They all tend to look at the same things. And when they see something important, the information spreads fast.

For that reason, I don't think we are going to receive clear danger signals or sell signals when this bull market breathes its last. No, it's not going to be that easy. Then how will the next bear market begin?

I think it will begin unexpectedly -- "out of the blue," as the market simply falls of its own weight. I think one day the market will simply topple over and head down. The decline may start very innocently with maybe a six or 10 point drop in the Dow. But the decline will be persistent and after three or four weeks a few leading analysts will sense that the top has passed. After that the news will spread and the decline will take on a nastier tone. Then slaughter will spread across the board, and the most frightening part will be that it will hit the mutual funds. The funds, I believe, will be decimated.

The creation and selling of mutual funds over the past few years has been almost beyond belief. Last year alone saw the emergence of 600 new mutual funds. On top of that, last year saw $72 billion in new corporate offerings. The public has been piling into the mutual funds, firmly believing that somehow their money was "safe" because the funds "are under professional management." At present, it looks as if fund buying will shoot up to a record rate of $10 billion a month. In 1991 the public bought $38.3 billion of stock mutual funds alone. In 1992 the total careened to $77.8 billion. That total will almost surely be exceeded this year.





I know there are a lot of arguments (there always are) against a bear market starting anytime in 1993. One very important argument is that this market has been trading off low (declining) interest rates -- and interest rates are still very low. There have been few instances where a market has collapsed with interest rates in a downtrend or holding at a low level.

True enough, but everyone knows about today's bullish interest rate picture. And everyone points to the bullishness of the Fed's current stance. So I say be careful, it's just too obvious. I say that when you're paying over $35 for a dollar of S&P dividends, the market's sky-high, and it can fall of its own weight. In fact, if this market starts falling, we could have a liquidity crisis as billions of dollars in values are wiped out. Such a liquidity crisis could (surprise) drive rates up -- and this after a bear market had started.

Question: What has generated the current stock market frenzy? Answer: A number of items have created the heat. First, the Fed has lowered interest rates to basement levels, causing tens of thousands of the public to cash in their CDs and move the money into the market via mutual funds.

Next, I think the public just got tired of being worried and bearish. After all, they had witnessed massive lay-offs by hundreds of corporations, they had watched company bankruptcies to the tune of 2,000 a week, they had heard endless warnings about city, state and federal deficits, they had watched the S&L disaster, they had seen the collapse of commercial real estate. In short they had read bad news in the newspaper and had seen bad news on TV day after day, week after week.

And lo and behold, the market had absorbed all the bad news and had either held or pushed higher. Could anything stop this market from climbing ever higher and ever onward? It didn't seem so. And the public buying of mutual funds increased from a stream to a river to a virtual torrent.

Then, along came the final plus -- Bill Clinton. At first he was distrusted and maligned -- "Slick Willy," the adulterer, the double-talker. Then, miracle of miracles, he was transformed by the press into William Jefferson Clinton, the golden baby-boomer president, the man of the people, the shining knight who will save America.

My old pal, Harry Schultz, put it well in his latest report, written from Europe. "The most treacherous new element in the world economic balance is the monumentally high expectations of a Clinton presidency (not only in the US but even my European barber has those expectations). It's based on hope and even desperation, not facts. Nobody could live up to those hopes. And Clinton has few options (at least among those he'll consider, or will be allowed to consider by the establishment). His room to maneuver is nil. Thus, there'll be an horrendous psychological let down within 3-6 months when Clinton can't turn wine into water. Confidence will plummet and retail sales will shrink. It'll turn a positive momentum into a negative one. It will probably coincide with the end of the mini-US recovery now underway, at midyear."

Bob Prechter of Elliot Wave fame, in his latest report, writes as follows: "Indeed, the word 'optimism' is an understatement in today's psychological climate . . . What is particularly remarkable is that the optimism of early 1993 is so powerfully entrenched despite the fact that the actual performance of the economy is substantially worse than it was four years ago. In other words, the disparity between actual performance and expectations is being stretched to the limit."

CONCLUSION: Stocks at this point are super-expensive; despite this the public continues to load up with equities via mutual funds. I don't know if you could call the mood in the markets wild or frenzied. But I would certainly label the mood of today -- COMPLACENCY with a capital C. The public is just not worried about the markets. They have been conditioned to buy all reactions. They have been conditioned to hold stocks through any reaction on the thesis that in due time the market will rise to new highs, taking their stocks with them. Complacency today in history's most expensive market -- it's remarkable.

COMMENTS: (1) It had to happen. On Feb. 8 The *WSJ* published an article headlined, "Low Dividend Yield May No Longer Be The Red Flag For Stocks It Once Was." Russell comment: Yeah, we know -- this time it's different.

(2) Watching the market a few weeks ago I got a feeling of deja vu. Back in the early 1970s the price of gold was $35 an ounce. That was at the beginning of the gold bull market. By late-'79 (with the bull market in high gear) we saw days when gold would be up $35 and $40 in a single day. In late-1974 when the bull market in stocks started the Transportation Average was 125. Then a few weeks ago we saw the Transports advance 73 points in the space of four days. That was a rise equal to 58% of the entire Transport Average when the bull market began. As I said, deja vu, but, of course, it may not mean anything.

(3) I can't imagine business being thrilled by Clinton's new plans for raising corporate taxes. The costs will be passed on to the consumers.

INVESTMENT POSITION: With new highs in the Dow and the Transports, the bull belongs in the box. A lot of people have asked me if we just received "a new Dow Theory buy signal." I told them "No, the recent action should be taken as a reconfirmation of the bull market, but with stock yields below 3% it's not a buy signal." There's a big difference between the reconfirmation of a bull market and a buy signal. Those who want to understand this will -- those who don't want to will continue to load up on mutual funds.

My perception is that we are closing in on a period of major change. I think the dollar could be topping, I think bonds are topping, I think gold is bottoming, I think there's a good chance the stock market is topping. Mind you, I can't prove any of this yet, but for what it's worth this is what I suspect.

If I'm correct, then for the majority of subscribers, the best place to be is in cash or equivalent. I'm still getting many letters asking about German bonds (bunds). The bunds have been in a steady rising trend, but due to the weak D-mark, gains for US holders have been wiped out despite bund strength. However, since I think the D-mark is now bottoming, I also think this is a pretty good spot to buy bunds. Where do you buy them? Well, I bought mine at both Merrill and Shearson.

As an added thought, the consensus thinking has been that the US economy will be improving all year, the stock market will continue to head up, and the dollar is in a bull market. I have serious doubts about all three of these opinions. I think Clinton (and his policies) will turn out to be a major disappointment. I agree with George Will (Feb. 10 column) when he writes, *"A pitched battle, we are told, rages within the administration between two factions, one wanting tax increases to cut the deficit, the other wanting spending to stimulate the economy. The predictable compromise will be: Taxes up, spending up, the deficit up."* Russell comment: Believe it.

NOTES & QUOTES: China is coming on. China's positive trade balance with the US now amounts to $2 billion a month, meaning that they sell us $2 billion a month more than we sell them. From 1985 to '90 Chinese industrial production increased 85%. Chinese holdings of foreign exchange now amount to $45 billion, almost four times that of 1985, nearly double France's and 75% of Japan's (figures courtesy of *Peter Bernstein, Inc,* NYC).

The Chinese like gold, they dislike debt, and they are obsessive savers. The Chinese have a long history of being frugal and good at business. So far they have been pictured as a potentially huge market of 1.1 billion buyers. Russell view: I see them as the coming super-competitive suppliers of goods to the world. Item: at the Super Bowl everyone was given a package of cards, maps, and hype plus a little radio with ear phones. I looked at the radio carefully -- and spotted the words, "Made in China."

* *

Speaking of bowls and sporting events, the World Cup of soccer is coming to the US in 1994. Soccer is the favorite sport of most of the world outside the US. A dozen US sponsors (Coke, McDonald's) are shelling out up to $20 million each for this event. Nine major US cities will host 52 matches, and the final World Cup will be played in Pasadena's Rose Bowl before a monster world audience of 1.5 billion TV viewers. The problem: how to sell 3.5 million US game tickets when most of the teams won't even be US teams. World Cup fans claim that soccer will be the sport of the '90s. Will the US love it? We'll see (although school kids throughout the US are now showing increased interest in soccer).

* *

This from old friend Eliot Janeway (17 E. 80 St., NYC 10021): "Too good to be true. As we won't be long discovering, the conclusion that our deficit troubles are behind us is just that. As a practical matter, there is no way in the world that Clinton can persuade his Democratic Congress to vote a tax on consumption big enough, and above all free enough from corporate exemptions, to make a plausible start at deficit reduction. Just watch any effort to do so turn the economy from a minimal muted recovery into an angry across-the-board collapse."

In Memorium: After I inserted the above, I heard that my old friend, Eliot Janeway, had died at the age of 80. Eliot was a long-time observer of the economy and the markets. He had been a writer for *Time* magazine, and later he wrote a weekly business letter for the personal use of Time/Life founder, Henry Luce. Eliot became a confidant of Lyndon Johnson's, but later broke with him when he disagreed violently with Johnson's "non-financing" of the Vietnam war.

Eliot was a great teacher, a man who consistently read through the nonsense that comes out of Washington. I'll sorely miss his weekly reports. My guess is that Eliot's up there somewhere, and if there's any nonsense in heaven, you can be darn sure that Eliot will root it out. Good bye, Eliot, adios.

* *

On the week ending February 5, I received a lot of calls from newspapers, TV and radio stations, all asking me what to make of the new highs in the averages. One of my pet peeves (and this is particularly true of the newspapers) is that reporters call who have little or no idea of what the stock market is all about. They've never taken the trouble to study it, but they're expected to write a story on the market (I might as well try to write a story on Sanitation Methods in Zaire). *USA Today* (Feb. 4) had a picture of me with the headline, "Analysts Deflate the Dow Theory." The article had almost nothing to do with what I said, and the writer just got it wrong. What do they say -- write anything you want as long as you spell my name right. That's about it. It's all very stupid, and it shows you how skeptical you have to be regarding what you read in the newspapers.

* *

Gambling anyone? Gross revenue from legal gambling in the US in 1991 amounted to $26.7 billion. This is five times the amount of the entire US box office from movies. The gross from illegal gambling is also huge, maybe larger than the legal gross. No wonder they keep building those monster hotel-casinos in Vegas.

* *

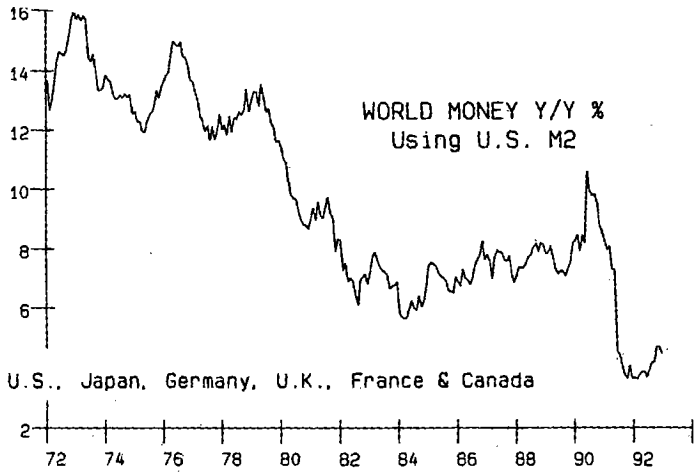
From William Safire's column in the Feb. 8 *NY Times*: "Let me let you in on a dirty little secret: No Democratic economist will ever admit this, but they don't think inflation of about 5% or 6% is such a bad thing. It would rescue real estate, which in turn would bail out banks and insurance companies now hung up on bad real estate loans. 'Reasonable' inflation would also allow government to reduce the deficit with cheaper dollars."

* *

From syndicated columnist Paul Craig Roberts in *Business Week:* "The Clinton Administration is setting itself up for early failure. It is planning to raise taxes in the name of lower deficits, and it won't work. Reagan and Bush tried to buy budget deals with tax increases, and each time the deficit rose. Now the new Administration can't wait to commit the same folly. The (higher) taxes will wreck people's living standards, the economy, and the Democrats' political fortunes. The question is whether the Republicans will prevent their own comeback by providing bipartisan cover . . . The broad-based energy tax sought by Democrats will lift costs and the measured rate of inflation -- which may prompt more Fed tightening. Look for Clintonomics to bring back stagflation." Russell comment: The comments about Clinton's "spend, then tax" policy are now so frequent and so negative that I wonder if he is going to go through with it. Mmmm, the way things are going, nothing would surprise me.

* *

Has the "Long (deflationary) Wave" got the world in its icy grip? *Financial World* magazine's February 16 cover story is entitled, "The Global Cash Shortage." The article starts, "Where has all the money gone?" This chart from Ed Hyman's *ISI* might ask the same question. In nation after nation we see the move to reflate and to lower interest rates. The rush is on to "un-squeeze" the money squeeze. Note: in the US the broad M-3 money supply is still not expanding on a year-to-year basis.



* *

Say It Isn't So, Bob: This piece isn't exactly happy news, but the new leader of the Republican party (where's George Bush?) said it, so it's worth pondering.

Dole doubts Democrats will wield knife

By Judy Keen
USA TODAY

Sen. Bob Dole predicts Democrats in Congress will cave to political pressure and refuse to trim Social Security benefits to cut the federal deficit.

"We're going to end up cutting defense and putting in higher taxes and that'll be about the end of it," the Senate minority leader said Wednesday of President Clinton's deficit reduction proposals.

"There won't be any tough choices made."

Dole said he'd support a reduction of Social Security cost-of-living raises to trim the $327 billion budget deficit if it's done on a sliding scale so the poor would not be affected.

Senior citizens' groups geared up their potent lobbying machines this week after the Clinton administration floated the idea.

"Democrats are jumping overboard pretty fast," Dole said. "It's difficult for Democrats who have been for 12 years nothing but opposition representatives to be responsible in some of these areas."

* *

I remember the Transportation Average at the 1974 low of 125. Then in 1989 it hit a record high of 1532.01. It sagged for the next four years, but last week it broke out to new highs. What or who took it up there? These stocks (all in the Transportation Average) did the real work. Here are the percentage rises from the 1992 lows: XTRA up 87%; Airborn Freight up 81%; Federal Express up 55%; Southwest Air up 51%; Conrail up 47%; Consolidated Freight up 44%; Burlington Northern up 42%; Ryder System up 34%; CSX up 33%. The airlines were the laggers, adding very little to the Transport "explosion."

* *

From *Sindlinger* (405 Osborne Land, Wallingford, PA 19086) : "In April 1991 the university professors, the ones who 'referee' business cycles, announced 'the recession' started in July 1990. Then, in December 1992 the 'referees' said that 'the recession' ended in March '91. This means it ended one month before they knew it had begun." Russell comment: As subscribers know, the blather from economists and university professors is useless as far as investing in the stock market is concerned. It is probably just as useless for businessmen. As a rule, the professors don't know where we're going. In fact, most don't even know where we've been.

* *

What are the top purchases (in dollars) sold by US supermarkets? The answer is a shocker. Here they are: (1) Marlboro cigarettes; (2) Coke Classic; (3) Pepsi; (4) Kraft Processed Cheese; (5) Diet Coke; (6) Campbell's soup; (7) Budweiser beer; (8) Tide detergent; (9) Folgers coffee; (10) Winston cigarettes. In other words, of the top 10 sellers, only two were foods. And the super market winners in America are -- ta da -- nicotine, caffeine and alcohol.

* *

A seat on the NYSE just sold for $575,000, up $75,000 from the last sale which took place on January 13. How's this for a spread -- the current bid for a seat is $550,000, while the offer is $1,000,000.

* *

Where are the jobs in the US? Here are some items: from 1970 to 1990 computer analysts increased from 107,580 to 471,290; dietitians increased from 43,275 to 635,911; finance managers from 220,483 to 635,911; food service from 3.3 million to 5.7 mils.; lawyers from 288,478 to 779,471; physicians from 296,900 to 586,715; police officers from 427,607 to 822,667. But jobs fading away are barbers, domestics, elevator operators, English professors, farmers, rail workers, shoe repairers, tailors, textile workers, tool & dye makers.

* *

One of my pet peeves is Congress' gall in exempting itself from many of the lousy laws you and I have to live with (including Social Security, yeah they have their own excellent pension plan). This from the Feb. 8 *WSJ*: "Now, needless to say, Congress has effectively exempted itself from the new Family Leave Act. As with the Civil Rights Act and the Americans With Disability Act, congressional employees cannot sue for damages in a federal court. So-called enforcement of the act in the House has been left to an 'Office of Fair Employment Practices,' which is made up of (surprise!) House Members. All of its meetings are closed, and none of the evidence it considers is ever made public. In effect, the House serves as prosecutor, judge and jury for any complaints filed by its more than 12,000 employees. Imagine if a Fortune 500 company tried something like this."

* *

Now this is interesting. According to a piece in the *International Herald Tribune*, the rumor is going around Germany and France that the US in concert with Britain is trying to torpedo the concept of a single European currency. The US fear, obviously, that a strong Euro currency would compete and maybe be preferable to the dollar. Remember, the US is the only nation which can pay back its debt with its own currency. If the US was ever to lose reserve currency status, you'd be selling your Treasury bonds for 75 cents on the dollar. Which reminds me, with help from US advisors, the Russian ruble has now gone down the drain. It is literally worthless. Why didn't advisors tell the Russians to back their ruble with gold? Maybe because the dollar is a paper currency, and the US didn't want another major currency going to gold backing. Ah, enough US advisors (probably from Harvard) can destroy any currency.

* *

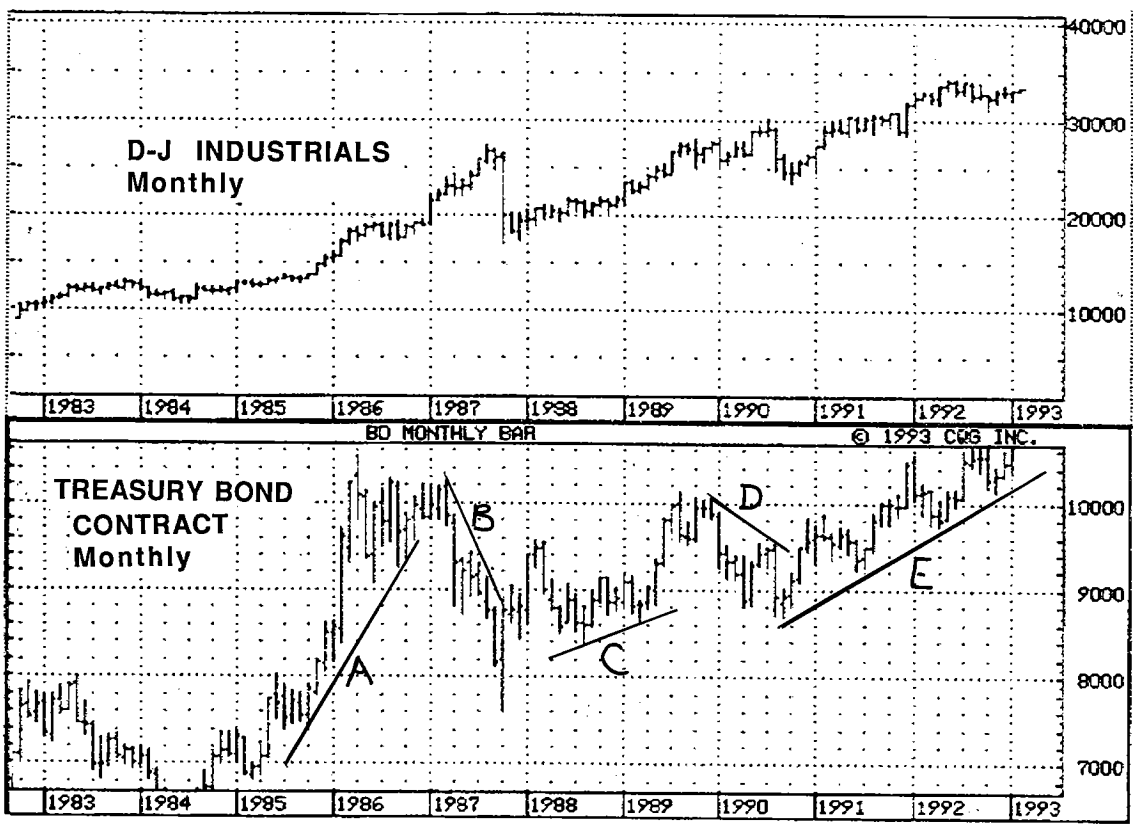
What does the new Washington power structure look like? Well, aside from Hillary, Clinton meets daily with only three advisors. White House Chief of Staff Tom McLarty, National Security Advisor Anthony Lake, and last but definitely not least, Robert Rubin. Rubin, former CEO of Wall Street's mighty Goldman Sachs, is one of the richest men in Washington with a fortune estimated at $50 million. Look for Rubin to be a power. He is described as slightly liberal on social issues, and relatively conservative on economic affairs.

STOCKS, BONDS, INTEREST RATES: I've been saying that the stock market has been trading off the interest rates, and if there's any doubt about that assessment this chart should remove those doubts.

The top section of the chart shows the Dow monthly, high, low and close. The bottom section of the chart shows the bond contract. Here, if the bonds are in a rising trend then interest rates are declining, and conversely, if the bonds are in a declining trend then interest rates are rising.

Let's follow the action on this chart. During 1985 and '86 the bonds were rising (trendline A on chart) and the Dow was rising with the bonds. But in March 1987, the bonds topped and headed sharply lower (B on chart). The interest rate pressure increased, and in October the market crashed (remember?).

During 1988-89 (C) bonds headed up again, rates declined and the stock market headed higher. But during early 1990 (D) bonds declined again and the market sank in August-October 1990.



Starting in mid-1990 (E) bonds headed higher as the Fed panicked and pushed interest rates down. The stock market responded, and as this is written rates are still low with the rumor being that the Clinton/Greenspan "alliance" may even be thinking of another cut in the discount rate.

NOTICE: The **1992 pages** for the D-J Averages chart book and the Advance-Decline ratio chart books are now off the press. Price is $3 per page. Readers who have not seen the chart books and would like a description, simply drop me a note, and we'll do the rest.

GOLD: Jim Cook of *Investment Rarities* (Minneapolis) provides a little background. "Of all the gold mined in history (estimated at 94,000 metric tons) about 80% is still accounted for. If collected in one block, it would cover one football field to the depth of about five feet. At the current price of $330 an ounce, its value would be something on the order of $600 billion. Most of the gold would never come on the market (it's held in central bank vaults, etc.) and the new gold (about $22 billion a year) is currently consumed in fabrication. So only a few billion dollars of buying would drive the price crazy." Russell comment: I find it interesting that the value of all the gold in the world is less than two years of US deficits.

So much for background. I don't know whether it's the Kondratieff down-wave or something else, but the world has been struggling with deflation and a shrinking global money supply. This has resulted in almost every nation in the world (except Germany) trying to reflate. On top of that, currency after currency has been devalued, and I find myself wondering how long it will be before the Forex traders get around to attacking the dollar -- the dollar with its low, low interest rates and screaming deficits.

The whole background is becoming increasingly interesting for gold. I don't see any strong US action on deficit reduction (where are the BIG spending cuts?), the Fed is pumping, the philosophy is low interest rates (and a cheap dollar), and let's face it -- everyone is waiting breathlessly for the US money supply to start expanding. Finally, the ratio of gold stocks to bonds has turned up in favor of gold, one of the most sensitive early barometers of inflation.

Important: Up to now the "strong" currencies provided an alternative to gold (and they paid interest as well). But with competitive devaluations and with the recent decline in the D-mark and Swissie, that leaves only the dollar as the supposed "island of safety." Ah yes, but with the Democrats in control of Washington and the US' predilection for a cheap dollar -- gold becomes more and more the only money that can legitimately be called a store of value.

Yep, we're even seeing some action in the metals. Palladium is very strong, platinum is waking up, and gold is trying to break upside from one of its tightest formations of the last twenty years. I watch XAU, the gold and silver stock index, and it's been advancing, almost daily. Since gold stocks often move before the metal, and since general investor sentiment regarding gold is still cold, cold, icy cold, I think we're nearing the time when the metal could shock everyone and head -- UP.

For subscribers who don't have any gold items, here's the menu. Very conservative subscribers buy the coins; for those who believe what I've written above, buy Amer. Barrick, Placer Dome, Royal Oak Mines (the last on the AMEX) and maybe even ASA. For dyed-in-the-wool gold bulls, add the December 370 gold calls (then if gold hits 400 by December, send me a gift but nothing too large -- only kidding, only kidding).

Note: The CBOT will be taking over the Comex. The merger is an admission that the Comex's core markets, gold and silver, have been losers for years. Brokers on the Comex were dying. Talk about the ultimate contrary opinion, even the precious metal pros can't make a living buying and selling the precious metal contracts. Russell adage: "It's time for buying when the pros are dying."

Potential shock of the year -- gold moves up, scaring the bonds which head down, and that in turn scares the market which heads down.

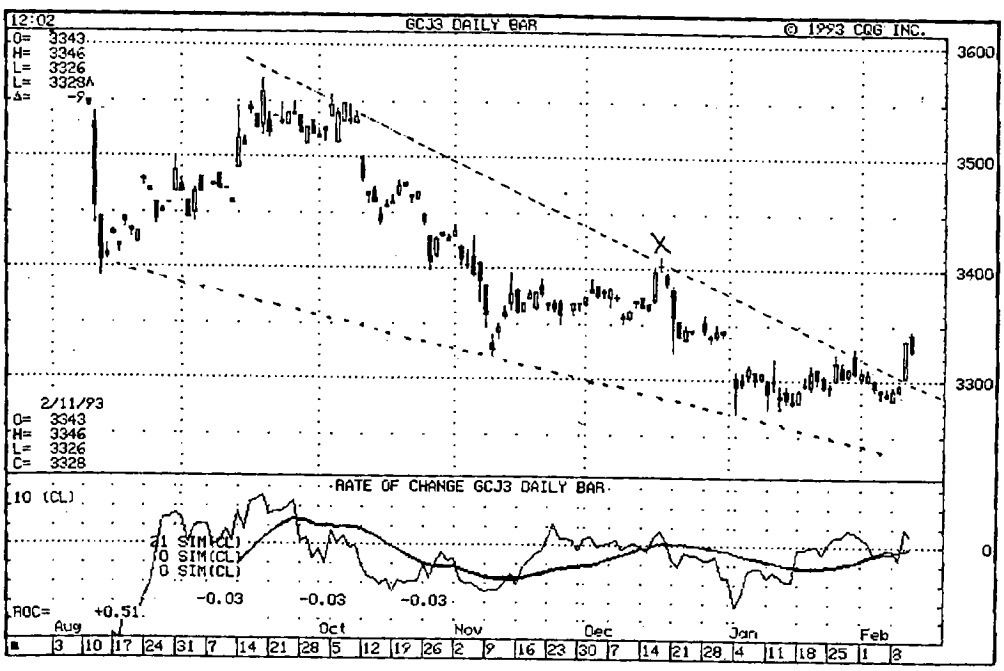
The chart below shows the April gold contract (daily). It's a Japanese candle stick chart, which means that the black bars are days of declines and the white bars are days of advance. Actually, I've grown to like the candle stick method of depicting price action -- it shows what's happening much more graphically than a simple bar line chart. The Japanese have a very definite method of reading candle stick charts, which I won't go into now.

What we see here is a large falling wedge pattern. A falling wedge usually represents a pattern of diminishing selling. Towards the apex of the wedge the price usually breaks to the upside (the reverse is true of a rising wedge pattern).

And sure enough, on February 10 we saw gold break out of its upper trendline. This is a hopeful development for gold-philes. A really bullish move would entail the April gold contract pushing above the 340 level, a level corresponding to the last peak (marked X on the chart).

LATE NOTES: The currencies are particularly interesting here. The Japanese yen has moved strongly up against the dollar. Japan has a very positive trade balance, a high savings rate and almost no government deficit to speak of. Japan's trade balance, in fact, is so positive that it is an embarrassment to the Japanese government. Therefore, both the US and Japan are desirous of a higher yen, which is what we're getting. Remember, a higher yen is worth more dollars -- and since Japan is a major importer of oil, the stronger yen cuts down their oil bill considerably. They love that.

As for the D-mark and the Swissie, they're a bit of a puzzle now. Both have come down hard against the dollar in recent months. But at this point, they're both oversold. Thus, they go down very reluctantly, but at the same time when they try to rally it's a struggle. Result -- a stand-off and little movement. The pound -- I've said all along the pound is worth a dollar and a quarter if that. And that's where I think it's heading.



The stock market? Tired on the upside, but I'm not certain that it's ready to go down.

FINAL: In closing I'm getting darn tired of hearing Clinton claiming that "he didn't realize how large the deficits were." C'mon, every thinking person knew that Bush's deficit figures were garbage. Clinton used the "lower taxes" bunk to get himself elected. And now the flip-flop with higher taxes to come. My reaction -- Ugh!

NEXT MAILING: Mar. 3, 1993